Finance and Resources Committee

3.00pm, Tuesday, 4 December 2018

Treasury Management: Mid-Term Report 2018/19

Item number	7.8
Report number	
Executive/routine	
Wards	
Council Commitments	

Executive Summary

The purpose of this report is to give an update on Treasury Management activity undertaken in the first half of 2018/19.

In accordance with the Strategy set in March 2018 the Council drew down no borrowing during the first half of the financial year and continued to fund capital expenditure temporarily from cash deposits. However, the Council did agree a forward starting loan of £60m which the Council is committed to drawing down in October 2020 and which manages an element of the Council's future interest rate risk. The overall approach continues to generates significant short-term savings in Loans Charges for the Council.

The investment return for 2018/19 continues to show out-performance against the Fund's benchmark, although low in absolute terms, while maintaining the security of the investments as a priority.

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Report

Treasury Management: Mid-Term Report 2018/19

1. Recommendations

1.1 It is recommended that the Committee:

1.1.1 notes the mid-term report on Treasury Management for 2018/19;

1.1.2 approve the changes to the Treasury Cash Fund Treasury Management Policy Statement;

1.1.3 notes the forward borrowing undertaken by the Council; and

1.1.4 refers the report to City of Edinburgh Council for approval and subsequent remit by the City of Edinburgh Council to the Governance Risk and Best Value Committee for scrutiny.

2. Background

2.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Sector, and under the code, the mid-term report has been prepared setting out activity undertaken.

3. Main report

3.1 **UK Interest Rates**

3.1.1 During the last six months, the Bank of England's (BoE) Monetary Policy Committee (MPC) made no change to monetary policy at its May and June meetings and then in a unanimous vote, increased UK Bank Rate from 0.50% to 0.75% in August. The Monetary Policy Committee made no change to Quantitative Easing (QE) which remains at £435bn. The MPC did note at the meeting of the 21st June that it now intends not to reduce its stock of purchased assets until the Bank Rate reaches around 1.5%. The previous guidance was around 2%, and the stock will be reduced at a gradual and predictable pace.

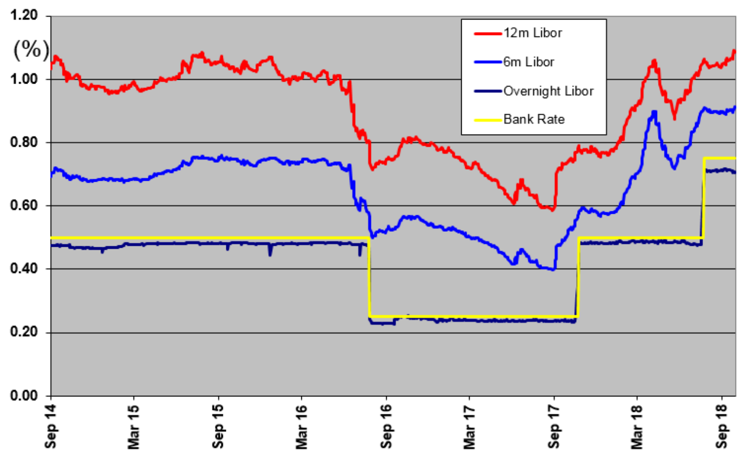

Figure 1 – Libor rates since September 2014

Source: Reuters

As can be seen in Figure 1 Libor rates increased anticipating the increase in UK Bank Rate in August. The shorter rates have since mainly levelled off with a slight increase in the 12-month rate anticipating a further increase in Bank Rate during the first quarter of 2019.

3.1.2 Table 1 gives a Reuters poll of up to 80 economists, taken 15th October, showing their forecasts for UK Bank Rate until Quarter 1 2020. This showed most economists polled believed that the UK Bank Rate will remain at 0.75% through Q1 2019 then increasing to 1% during Q2 2019 and to 1.25% in Q1 2020.

	Q4/18	Q1/19	Q2/19	Q3/19	Q4/19	Q1/20
Median	0.75	0.75	1	1	1	1.25
Mean	0.75	0.78	0.88	0.96	1.05	1.11
Mode	0.75	0.75	1	1	1	1.25
Min	0.75	0.75	0.75	0.75	0.75	0.75
Max	0.75	1	1	1.25	1.25	1.5

Table 1 – Economists' Forecasts for UK Bank Rate

Source: REUTERS

3.1.3 The annual rate of inflation (CPI) was 2.4% in September 2018, a decrease from 2.7% in August and above the Bank of England's target rate of 2%. CPIH (Consumer Prices Index including owner occupiers' housing costs) decreased slightly from 2.4% in August to 2.2% in September. Food and non-alcoholic beverages were the largest downwards contributors to inflation with transport, recreation and culture, and clothing and contributing to the decrease.

3.2 **Investment Out-turn**

3.2.1 The Council's cash balances are pooled and invested via the Treasury Cash Fund subject to the limits set out in the Treasury Management Policy Statement. Figure 2 below shows the daily investment in the Cash Fund since April 2009 The Treasury Management strategy is to ensure that surplus funds are invested in accordance with the list of approved organisations for investment, minimising the risk to the capital sum and optimising the return on these funds consistent with those risks. The Cash Fund's Investment Strategy continues to be based around the security of the investments.

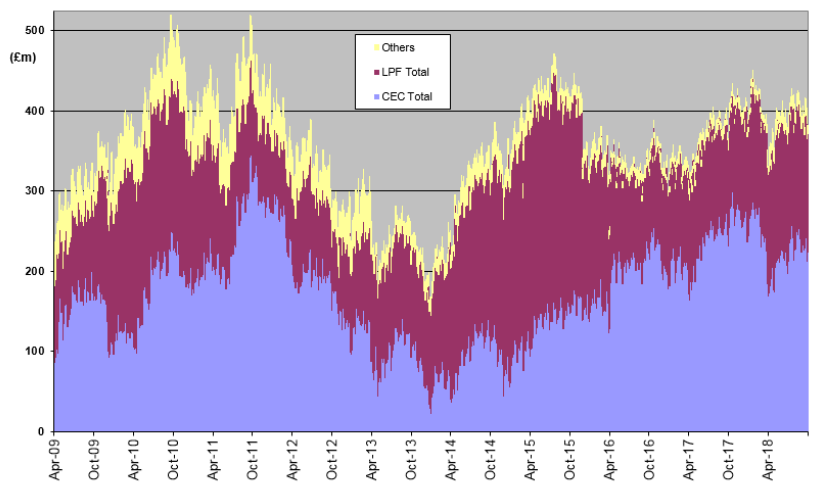

Figure 2 - Source of Funds

3.2.2 The rates achieved on the Council's call accounts have increased with the rise in UK Bank Rate. Although they are not all directly related so did not all change immediately. The rate on offer from the DMO's Debt Management Agency Deposit Facility (DMADF) was surprisingly high for deposits in excess of £25m and was used directly after the rise in Bank Rate for the first time since 2012. Figure 3 shows the rates achieved in the Friday auctions of UK Treasury Bills. Treasury Bill yields also increased with the increase in UK Bank Rate and proved useful in providing an uplift in rate while money market funds caught up. The amount of Treasury Bills was increased through to the end of the quarter with the holding reaching £90m at an average interest rate of 0.69% with the highest rate achieved being 0.719%.

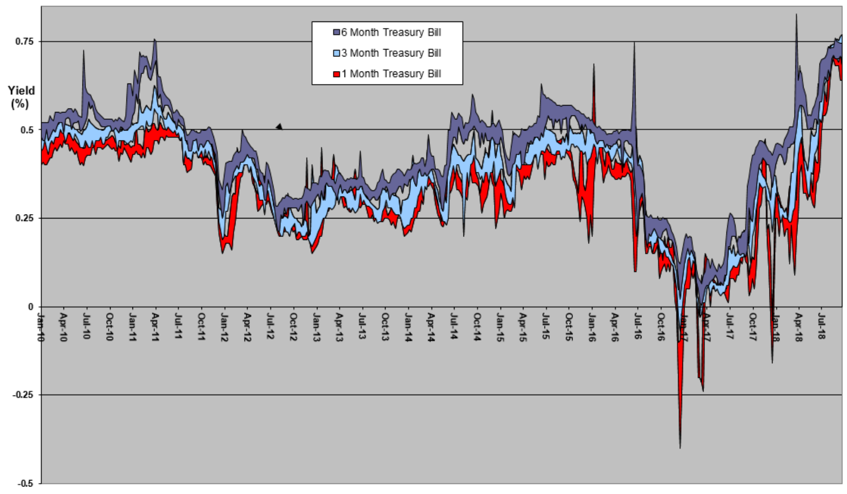

Figure 3 – UK Treasury Bill Yields

Source: DMO

3.2.3 Figure 4 shows in detail the distribution of Cash Fund investments since inception in 2007. This continues to show the fund retaining a large percentage of local authority deposits and also the investment into UK Treasury Bills.

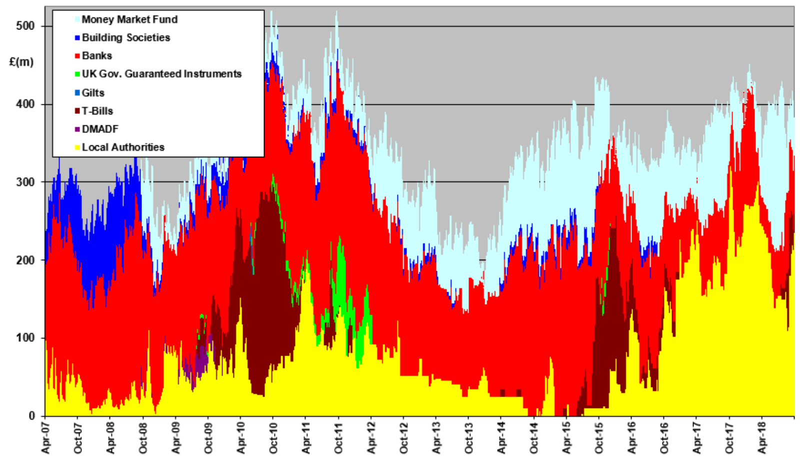

Figure 4 – Cash Fund Investments since inception

3.2.4 As can be seen in Figure 5, 65.4% of the fund was invested in Local Authority deposits between 23 different authorities, 6.5% invested in UK Treasury Bills, 19.5% was invested with Banks in call accounts split between instant access and 31 day notice with HSBC and 8.6% on deposit with Money Market Funds.

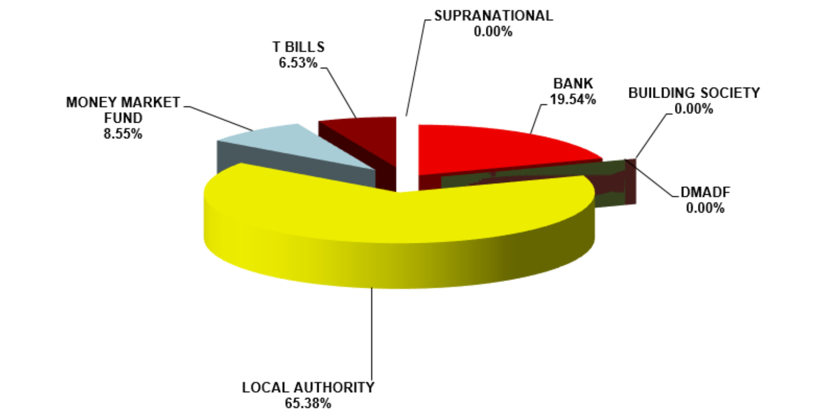

Figure 5 – Investments by Counterparty 30 September 2018

3.2.5 The investment strategy was based round the increase in UK Bank Rate in August. As anticipated the MPC increased rates at the start of August; as can be seen in Figure 6 the fund was perfectly profiled to take advantage of the rate increase. The low weighted average life of the fund allowed the cash fund to be able to react quickly to the hike in rates. Maturing deposits were placed on deposit at higher rates of interest and instant access money market funds allowed movement into bank call accounts that reacted instantly, UK Treasury Bills and Local Authority deposits. Notice was placed with Local Authority call accounts to increase interest rates which were agreed to and others increased the next working day with a clause that had been negotiated.

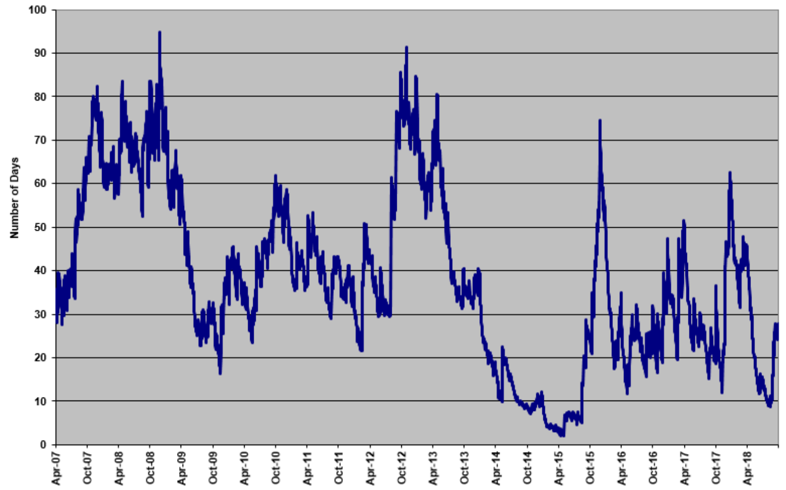

Figure 6 - Cash Fund Weighted Average Life

3.3 Cash Fund Performance

3.3.1 The annualised rate of return for the Cash Fund for the six months to September 2018 was 0.606% against a benchmark of 0.436%. Figure 7 below shows the daily investment performance of the Cash Fund against its benchmark since April 2011. As can be seen, Cash Fund performance picked up very quickly after the increase in UK Bank Rate. This was due to being able to move cash balances between accounts that had an instant uplift in rate from those that would take a while to catch up and also taking advantage of increased rates on fixed deposits with other Local Authorities, DMADF and UK Treasury Bills.

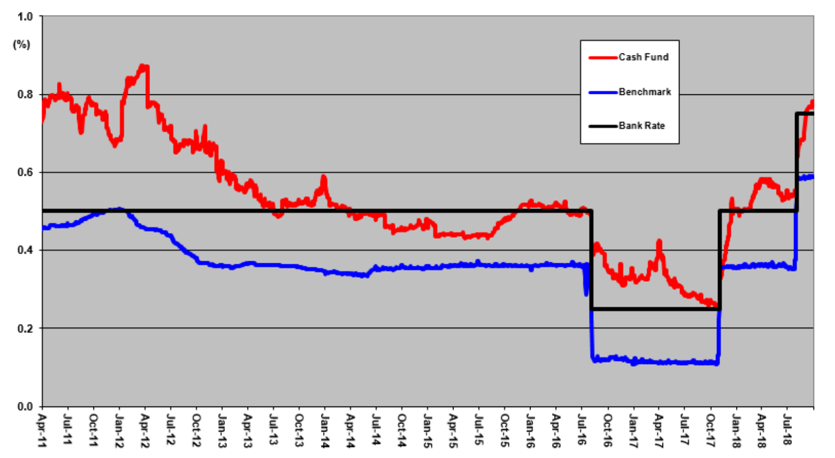

Figure 7 - Treasury Cash Fund Investment Performance

3.4 Debt Management Activity

3.4.1 Debt Management strategy for 2018/19 as outlined in the Strategy Report was to continue to use the Council's investment balances to fund capital expenditure. The Council has undertaken no PWLB borrowing since December 2012. Appendix 1 shows the current debt portfolio.

3.4.2 Figure 8 below shows the PWLB borrowing rates since April 2005. UK Gilt yields showed volatility in the first 6 months of the financial year – the 10 year gilt yield rising from 1.37% to 1.57% over the period. There was a sharp fall in yields in late May due to Italy's political crisis as the UK was viewed to be a safe haven.

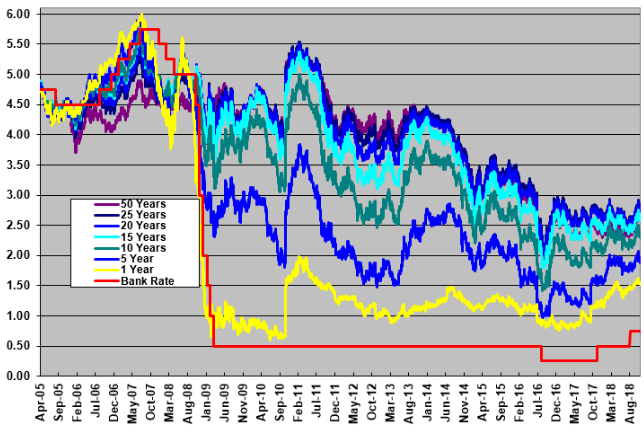

Figure 8 – PWLB Rates 2005 to Date

Source: DMO

3.4.3 Table 2 below shows a comparison of the projected cumulative capital expenditure to be funded by borrowing and the actual external debt. More detail on the Capital Advances, along with revised Prudential Indicators are contained in the Capital Monitoring – Period 5 report elsewhere on this agenda.

Capital Funding v. External Debt	**2017/18 Outturn £000**	**2018/19 Estimate £000**	**2019/20 Estimate £000**	**2020/21 Estimate £000**	**2021/22 Estimate £000**	**2022/23 Estimate £000**
Debt b/fd	1,299,901	1,245,546	1,203,456	1,329,875	1,474,308	1,527,070
Cumulative Capital Expenditure b/fd	1,413,522	1,384,534	1,402,260	1,561,620	1,719,428	1,782,363
Over/underborrowed b/fd	-113,621	-138,988	-198,804	-231,746	-245,120	-255,293
GF Capital Financed by borrowing	14,516	28,688	134,319	113,575	36,859	10,282
HRA Capital Financed by borrowing	35,078	20,742	76,268	50,416	44,927	24,100
Lending to LLPs		45,078	25,618	77,603	73,665	117,879
less scheduled repayments by GF	-57,810	-55,750	-54,540	-57,466	-62,688	-65,893
less scheduled repayments by HRA	-18,290	-19,457	-21,788	-25,776	-29,272	-33,368
less scheduled repayments by Joint Boards	-2,482	-1,575	-517	-544	-556	-589
less scheduled repayments by LLPs			-159	-1,123	-1,052	-1,897
Underlying Need to Borrow	**-28,988**	**17,726**	**159,360**	**157,808**	**62,935**	**52,412**
plus total maturing debt	54,355	54,960	53,581	55,567	47,238	46,505
Total Borrowing Requirement	**25,367**	**72,686**	**212,941**	**213,375**	**110,173**	**98,917**
Cummulative Borrowing Requirement		**72,686**	**285,628**	**499,002**	**609,175**	**708,092**
Committed Market Borrowing				**60,000**		
Planned PWLB or short borrowing for year	0	12,870	180,000	140,000	100,000	110,000
Debt at end of the year	**1,245,546**	**1,203,456**	**1,329,875**	**1,474,308**	**1,527,070**	**1,590,565**
Cumulative Capital Expenditure	**1,384,534**	**1,402,260**	**1,561,620**	**1,719,428**	**1,782,363**	**1,834,775**
Cumulative Over/Under Borrowed	**-138,988**	**-198,804**	**-231,746**	**-245,120**	**-255,293**	**-244,210**

Table 2 - Summary of Capital Advances v. External Debt

3.4.4 It is intended to continue the strategy of using investments to temporarily fund the Council's borrowing requirement giving a projected under borrowing of £199m at the end of the financial year. However, as set out in the 2018/19 Strategy, borrowing to mitigate the interest rate risk on the capital advances for the Edinburgh Living LLPs will be considered on a tranche by tranche basis. Some PWLB Borrowing in 2018/19 for this is therefore included in the above table.

3.4.5 As can be seen from Table 2 above, the Council's cumulative borrowing requirement is substantial over the next few years. Significant work has been undertaken to investigate ways in which the interest rate risk on this requirement can be managed and mitigated. As part of this, the Council has agreed a £60m forward starting loan with Deutsche Pfandbriefbank (PBB). The loan is to be drawn down in October 2020 and the fixed rate of 2.613% on the 25 year annuity loan is considered to represent excellent value to the Council in managing its interest rate risk without taking on a cost of interest rate carry.

3.5 Change to Cash Fund Treasury Management Policy Statement

3.5.1 The European Union has brought in some regulatory changes relating to Money Market Funds (MMFs) and existing funds are required to be compliant with them by 21 January 2019. The Council currently invests in Constant Net Asset Value (CNAV) MMFs. However, under the new regulations, after January this type of fund will only be permitted to invest in Government Debt. It is therefore thought likely that the funds which the Council currently uses will change to being Low Volatility Net Asset Value (LVNAV) funds. The Cash Fund's Treasury Policy Statements permits the use of MMFs. Although there was no reference to CNAV in the list of Permitted Investment in the Policy Statement, item e. in table outlining the risks associated with each investment type stated that the Council would only use CNAV funds. Item e. has therefore been amended to remove the reference to CNAV funds and reflect the Council's likely usage of the LVNAV funds. A revised Treasury Cash Fund Treasury Management Policy Statement is included in Appendix 2.

3.6 Edinburgh Living Facility

3.6.1 The Council has previously approved lending £13m to Edinburgh Living to fund its purchase of 105 homes. However, cash flow modelling for Edinburgh Living showed that as with most new enterprises, there is a timing mismatch in the early life of the enterprise between initial costs and when the income stream from rents is going to be fully received. Therefore, at its meeting on 11 October 2018 the Finance and Resources Committee approved providing a short-term cash flow facility of up to £0.25m to Edinburgh Living.

4. Measures of success

4.1 The success of the Treasury Section can be measured by the out-performance of the Treasury Cash Fund against its benchmark and managing the Council's debt portfolio to minimise the cost to the Council while mitigating risk.

5. Financial impact

5.1 The Council continues to manage its debt portfolio so as to minimise the medium-term cost of funding its capital projects.

5.2 The Treasury Cash Fund has generated significant additional income for the Council.

6. Risk, policy, compliance and governance impact

6.1 The Council complies with the relevant CIPFA code of practice whilst undertaking Treasury Management activities. The significant financial risks associated with Treasury Management activities have been successfully managed during the first half of 2018/19.

7. Equalities impact

7.1 There are no adverse equality impacts arising from this report.

8. Sustainability impact

8.1 There are no adverse sustainability impacts arising from this report.

9. Consultation and engagement

9.1 None

10. Background reading/external references

10.1 None

Stephen S. Moir

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11. Appendices

1: Outstanding Debt at 30 September 2018

2: Treasury Cash Fund Treasury Management Policy Statement

Appendix 1: Outstanding Debt at 30 September 2018

Market Debt (non LOBO)

Loan Type	Start Date	Maturity Date	Principal Outstanding (£)	Interest Rate (%)	Annual Interest (£)
M	30/06/2005	30/06/2065	5,000,000.00	4.4	220,000.00
M	07/07/2005	07/07/2065	5,000,000.00	4.4	220,000.00
M	21/12/2005	21/12/2065	5,000,000.00	4.99	249,500.00
M	28/12/2005	24/12/2065	12,500,000.00	4.99	623,750.00
M	14/03/2006	15/03/2066	15,000,000.00	5	750,000.00
M	18/08/2006	18/08/2066	10,000,000.00	5.25	525,000.00
M	01/02/2008	01/02/2078	10,000,000.00	3.95	395,000.00
			62,500,000.00		

Market Debt (LOBO)

Loan Type	Start Date	Maturity Date	Principal Outstanding (£)	Interest Rate (%)	Annual Interest (£)
M	12/11/1998	13/11/2028	3,000,000.00	4.75	142,500.00
M	15/12/2003	15/12/2053	10,000,000.00	5.25	525,000.00
M	18/02/2004	18/02/2054	10,000,000.00	4.54	454,000.00
M	28/04/2005	28/04/2055	12,900,000.00	4.75	612,750.00
M	25/02/2011	25/02/2060	15,000,000.00	7.411	1,111,650.00
M	25/02/2011	25/02/2060	10,000,000.00	7.411	741,100.00
M	26/02/2010	26/02/2060	5,000,000.00	7.381	369,050.00
M	26/02/2010	26/02/2060	10,000,000.00	7.381	738,100.00
M	01/07/2005	01/07/2065	10,000,000.00	3.86	386,000.00
M	24/08/2005	24/08/2065	5,000,000.00	4.4	220,000.00
M	07/09/2005	07/09/2065	10,000,000.00	4.99	499,000.00
M	13/09/2005	14/09/2065	5,000,000.00	3.95	197,500.00
M	03/10/2005	05/10/2065	5,000,000.00	4.375	218,750.00
M	23/12/2005	23/12/2065	10,000,000.00	4.75	475,000.00
M	06/03/2006	04/03/2066	5,000,000.00	4.625	231,250.00
M	17/03/2006	17/03/2066	10,000,000.00	5.25	525,000.00
M	03/04/2006	01/04/2066	10,000,000.00	4.875	487,500.00
M	03/04/2006	01/04/2066	10,000,000.00	4.875	487,500.00
M	03/04/2006	01/04/2066	10,000,000.00	4.875	487,500.00
M	07/04/2006	07/04/2066	10,000,000.00	4.75	475,000.00
M	05/06/2006	07/06/2066	20,000,000.00	5.25	1,050,000.00
M	05/06/2006	07/06/2066	16,500,000.00	5.25	866,250.00
			212,400,000.00		

PWLB Loan Type	Start Date	Maturity Date	Principal Outstanding (£)	Interest Rate (%)	Annual Interest (£)
M	17/09/1993	15/11/2018	5,000,000.00	7.875	393,750.00
M	23/03/1994	15/11/2018	5,000,000.00	8	400,000.00
M	14/03/1994	11/03/2019	2,997,451.21	7.625	228,555.65
M	18/10/1993	25/03/2019	5,000,000.00	7.875	393,750.00
M	30/03/2009	30/03/2019	5,000,000.00	3.46	173,000.00
M	21/04/2009	21/04/2019	10,000,000.00	3.4	340,000.00
M	23/04/2009	23/04/2019	5,000,000.00	3.38	169,000.00
A	12/11/2008	12/11/2019	815,196.27	3.96	47,699.55
M	23/03/1994	15/11/2019	5,000,000.00	8	400,000.00
M	07/12/1994	15/11/2019	10,000,000.00	8.625	862,500.00
A	01/12/2008	01/12/2019	804,410.88	3.65	43,433.85
M	01/12/2009	01/12/2019	5,000,000.00	3.77	188,500.00
M	14/12/2009	14/12/2019	10,000,000.00	3.91	391,000.00
M	15/02/1995	25/03/2020	5,000,000.00	8.625	431,250.00
M	21/04/2009	21/04/2020	10,000,000.00	3.54	354,000.00
M	12/05/2009	12/05/2020	10,000,000.00	3.96	396,000.00
M	21/10/1994	15/05/2020	5,000,000.00	8.625	431,250.00
M	07/12/1994	15/05/2020	5,000,000.00	8.625	431,250.00
M	21/11/2011	21/05/2020	15,000,000.00	2.94	441,000.00
M	16/08/1995	03/08/2020	2,997,451.21	8.375	251,036.54
M	09/12/1994	15/11/2020	5,000,000.00	8.625	431,250.00
A	10/05/2010	10/05/2021	1,534,840.41	3.09	58,602.91
M	21/10/1994	15/05/2021	10,000,000.00	8.625	862,500.00
M	10/03/1995	15/05/2021	11,900,000.00	8.75	1,041,250.00
M	12/06/1995	15/05/2021	10,000,000.00	8	800,000.00
M	02/06/2010	02/06/2021	5,000,000.00	3.89	194,500.00
M	16/08/1994	03/08/2021	2,997,451.21	8.5	254,783.35
M	28/04/1994	25/09/2021	5,000,000.00	8.125	406,250.00
M	23/04/2009	23/04/2022	5,000,000.00	3.76	188,000.00
M	12/06/1995	15/05/2022	10,200,000.00	8	816,000.00
M	14/06/2010	14/06/2022	10,000,000.00	3.95	395,000.00
M	31/03/1995	25/09/2022	6,206,000.00	8.625	535,267.50
M	16/02/1995	03/02/2023	2,997,451.21	8.625	258,530.17
M	24/04/1995	25/03/2023	10,000,000.00	8.5	850,000.00
M	05/12/1995	15/05/2023	5,200,000.00	8	416,000.00
M	20/09/1993	14/09/2023	2,997,451.21	7.875	236,049.28
M	20/09/1993	14/09/2023	584,502.98	7.875	46,029.61
M	08/05/1996	25/09/2023	10,000,000.00	8.375	837,500.00
M	13/10/2009	13/10/2023	5,000,000.00	3.87	193,500.00
M	05/12/1995	15/11/2023	10,000,000.00	8	800,000.00
M	10/05/2010	10/05/2024	10,000,000.00	4.32	432,000.00
M	28/09/1995	28/09/2024	2,895,506.10	8.25	238,879.25
M	14/05/2012	14/11/2024	10,000,000.00	3.36	336,000.00

A	14/12/2009	14/12/2024	5,005,280.81	3.66	201,656.97
M	17/10/1996	25/03/2025	10,000,000.00	7.875	787,500.00
M	10/05/2010	10/05/2025	5,000,000.00	4.37	218,500.00
M	16/11/2012	16/05/2025	20,000,000.00	2.88	576,000.00
M	13/02/1997	18/05/2025	10,000,000.00	7.375	737,500.00
M	20/02/1997	15/11/2025	20,000,000.00	7.375	1,475,000.00
A	01/12/2009	01/12/2025	8,108,232.64	3.64	320,458.85
M	21/12/1995	21/12/2025	2,397,960.97	7.875	188,839.43
M	21/05/1997	15/05/2026	10,000,000.00	7.125	712,500.00
M	28/05/1997	15/05/2026	10,000,000.00	7.25	725,000.00
M	29/08/1997	15/11/2026	5,000,000.00	7	350,000.00
M	24/06/1997	15/11/2026	5,328,077.00	7.125	379,625.49
M	07/08/1997	15/11/2026	15,000,000.00	6.875	1,031,250.00
M	13/10/1997	25/03/2027	10,000,000.00	6.375	637,500.00
M	22/10/1997	25/03/2027	5,000,000.00	6.5	325,000.00
M	13/11/1997	15/05/2027	3,649,966.00	6.5	237,247.79
M	17/11/1997	15/05/2027	5,000,000.00	6.5	325,000.00
M	13/12/2012	13/06/2027	20,000,000.00	3.18	636,000.00
M	12/03/1998	15/11/2027	8,677,693.00	5.875	509,814.46
M	06/09/2010	06/09/2028	10,000,000.00	3.85	385,000.00
M	14/07/2011	14/07/2029	10,000,000.00	4.9	490,000.00
E	14/07/1950	03/03/2030	2,906.90	3	87.21
M	14/07/2011	14/07/2030	10,000,000.00	4.93	493,000.00
E	15/06/1951	15/05/2031	3,046.64	3	91.40
M	06/09/2010	06/09/2031	20,000,000.00	3.95	790,000.00
M	15/12/2011	15/06/2032	10,000,000.00	3.98	398,000.00
M	15/09/2011	15/09/2036	10,000,000.00	4.47	447,000.00
M	22/09/2011	22/09/2036	10,000,000.00	4.49	449,000.00
M	10/12/2007	10/12/2037	10,000,000.00	4.49	449,000.00
M	08/09/2011	08/09/2038	10,000,000.00	4.67	467,000.00
M	15/09/2011	15/09/2039	10,000,000.00	4.52	452,000.00
M	06/10/2011	06/10/2043	20,000,000.00	4.35	870,000.00
M	09/08/2011	09/02/2046	20,000,000.00	4.8	960,000.00
M	23/01/2006	23/07/2046	10,000,000.00	3.7	370,000.00
M	23/01/2006	23/07/2046	10,000,000.00	3.7	370,000.00
M	19/05/2006	19/11/2046	10,000,000.00	4.25	425,000.00
M	07/01/2008	07/01/2048	5,000,000.00	4.4	220,000.00
M	27/01/2006	27/07/2051	1,250,000.00	3.7	46,250.00
M	16/01/2007	16/07/2052	40,000,000.00	4.25	1,700,000.00
M	30/01/2007	30/07/2052	10,000,000.00	4.35	435,000.00
M	13/02/2007	13/08/2052	20,000,000.00	4.35	870,000.00
M	20/02/2007	20/08/2052	70,000,000.00	4.35	3,045,000.00
M	22/02/2007	22/08/2052	50,000,000.00	4.35	2,175,000.00
M	08/03/2007	08/09/2052	5,000,000.00	4.25	212,500.00
M	30/05/2007	30/11/2052	10,000,000.00	4.6	460,000.00
M	11/06/2007	11/12/2052	15,000,000.00	4.7	705,000.00
M	12/06/2007	12/12/2052	25,000,000.00	4.75	1,187,500.00

M	05/07/2007	05/01/2053	12,000,000.00	4.8	576,000.00
M	25/07/2007	25/01/2053	5,000,000.00	4.65	232,500.00
M	10/08/2007	10/02/2053	5,000,000.00	4.55	227,500.00
M	24/08/2007	24/02/2053	7,500,000.00	4.5	337,500.00
M	13/09/2007	13/03/2053	5,000,000.00	4.5	225,000.00
M	12/10/2007	12/04/2053	5,000,000.00	4.6	230,000.00
M	05/11/2007	05/05/2057	5,000,000.00	4.6	230,000.00
M	15/08/2008	15/02/2058	5,000,000.00	4.39	219,500.00
M	02/12/2011	02/12/2061	5,000,000.00	3.98	199,000.00
			939,050,876.65		

SALIX INTEREST FREE

Loan Type	Start Date	Maturity Date	Principal Outstanding (£)	Interest Rate (%)	Annual Interest (£)
E	07/01/2015	01/09/2021	236,871.42	0	0.00
E	31/03/2015	01/04/2023	901,448.70	0	0.00
E	22/09/2015	01/10/2023	241,779.67	0	0.00
			1,380,099.79		

Appendix 2: Treasury Management Policy Statement

The City of Edinburgh Council

Treasury Cash Fund

Treasury Management Policy Statement

Summary

The Council operates the Treasury Cash Fund on a low risk low return basis for cash investments on behalf of itself, Lothian Pension Fund and other associated organisations. This Policy Statement covers the type of investments which are permitted for monies held with the Cash Fund and should be read in conjunction with the Treasury Policy Statement for the City of Edinburgh Council.

Approved Activities

The activity undertaken in the management of cash balances and their investment in cash and near cash instruments. In undertaking this activity, the key objective is the security of the monies invested. Accordingly, the investment types and counterparty limits below represent a prudent attitude towards the instruments with which and the institutions with whom investment will be undertaken.

Treasury Management Strategy

The treasury management strategy for the cash fund is to ensure that surplus funds are invested in accordance with the list of approved organisations for investment, minimising the risk to the capital sum and optimising the return on these funds consistent with those risks

Permitted Instruments

The Chief Financial Officer may invest monies in accordance with the Council's requirements only by using the following instruments:

(a) Temporary deposit, Certificate of Deposit, collaterised deposit, structured deposit, commercial paper, floating rate note or Bonds with an approved institution of the Bank of England or with any other approved organisation for investment (see below)

(b) UK Treasury Bills

(c) Gilt-edged securities

(d) Reverse Repurchase Agreements

(e) Money Market Funds and Bond Funds

(f) Debt Management Office's Debt Management Agency Deposit Facility

Limits on Investment

The approved limits on counterparties and investment types are as follows (where money limits and percentages are stated, the greater of the two should be applied):

(a) DMO's DMADF, UK Treasury Bills and UK Gilts with no limit

(b) UK local authorities with no limit.

(c) other public bodies up to a maximum of £20 million per organisation.

(d) The Council's bankers, where not otherwise permitted under (k) below, up to a limit of £20m on an overnight only basis other than when funds are received into the Council's bank account without pre-notification.

(e) Money Market Funds with no limit in total but with no more than £30 million or 15% of the funds under management with any one Fund.

(f) Bond Funds with no more than £20 million or 10% of the funds under management.

(g) Supranational Bonds with a limit of £60 million or 20% of the fund in total.

(h) financial institutions where the relevant deposits, CDs or Bonds are guaranteed by a sovereign government of AA or above up to a maximum of £60 million or 20 percent of the fund per institution for the duration of the guarantee in addition to the appropriate counterparty limit for the institution.

(i) Local Authority Collateralised deposits up to a maximum of £30 million or 15 percent of the fund per institution up to a maximum of 5 years in addition to the appropriate counterparty limit for the institution.

(j) Structured deposits up to a maximum of £20 million or 10 percent of the fund, subject to the appropriate counterparty limits for the institution also being applied.

(k) financial institutions included on the Bank of England's authorised list under the following criteria:

Credit Rating	**Banks Unsecured**	**Banks Secured**	**B. Socs. Unsecured**	**B. Socs. Secured**
AAA	20% or £60m	20% or £60m	20% or £60m	20% or £60m
AA+	15% or £30m	20% or £60m	15% or £30m	20% or £60m
AA	15% or £30m	20% or £60m	15% or £30m	15% or £30m
AA-	15% or £30m	20% or £60m	10% or £20m	15% or £30m
A+	10% or £20m	15% or £30m	10% or £20m	10% or £20m
A	10% or £20m	15% or £30m	10% or £20m	10% or £20m
A-	10% or £20m	15% or £30m	5% or £10m	10% or £20m
BBB+	5% or £10m	5% or £10m	n/a	n/a
None	n/a	n/a	n/a	n/a

The credit ratings quoted in the above table are for the financial institution, instrument or security provided and are the lowest of the relevant long term ratings from the three main Credit ratings agencies, S&P, Moodys and Fitch.

Time Limits

In addition to the monetary limits above, the following maximum time limits will be placed on investments:

Category	Max. Time Limit
20% of Assets Under Management / £60m	5 Years
15% of Assets Under Management / £30m	1 Years
10% of Assets Under Management / £20m	6 months
5% of Assets Under Management / £10m	3 months

In addition to the above limits, no more than 25% of assets under management will have a maturity greater than 1 year.

In considering an investment, consideration is given to a wide range of information, not simply the credit ratings of the institution being considered. This will include financial information on the institution, relevant Credit Default Swaps and equity pricing data, and the general macro-economic, market and sector background. The investment risks and controls to mitigate those risks are outlined to the end of this document.

Policy on Delegation

The Treasury Cash Fund is operated under the Council's Treasury Policy Statement and the delegations are defined in that document.

Reporting Arrangements

This will include, as a minimum, an annual strategy and plan in advance of the year, and an annual report after its close, in the form prescribed in its TMPs. The Head of Finance will report to the Council as follows:

(a) A Treasury Strategy prior to the commencement of the financial year.

(b) A mid-term report during the financial year.

(c) A Treasury Annual Report as soon as practicable after the end of the financial year.

(d) Ad hoc reports according to need.

Type of Investment	Treasury Risks	Mitigating Controls
a. Deposits with the Debt Management Account Facility (UK Government) (**Very low risk)**	This is a deposit with the UK Government and as such counterparty and liquidity risk is very low, and there is no risk to value. Deposits can be between overnight and 6 months.	As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments.
b. UK Treasury Bills **(Very Low Risk)**	These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates unless held to maturity. Maturity at issue is only 1, 3 or 6 months so will be used mainly in the 1 to 3 month period to provide a high level of security but a better return than the DMADF in (a).	As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments.
c. UK Gilts **(Very Low Risk)**	These are marketable securities issued by the UK Government and as such counterparty and liquidity risk is very low, although there is potential risk to value arising from an adverse movement in interest rates unless held to maturity. There is a risk to capital if the Gilt needed to be sold, so should only be used on a hold to maturity basis as a proxy for a slightly longer maturity Treasury Bill	As this is a UK Government investment the monetary limit is unlimited to allow for a safe haven for investments. Would only be used on a hold to maturity basis at the very short end of the yield curve.
d. Deposits with other local authorities or public bodies **(Very low risk)**	These are considered quasi UK Government debt and as such counterparty risk is very low, and there is no risk to value.	Little mitigating controls required for local authority deposits, as this is a quasi UK Sovereign Government investment.
e. Money Market Funds (MMFs) **(low/medium risk)**	Pooled cash investment vehicle which provides short term liquidity.	Funds will generally be used to provide liquidity for the Cash Fund.
f. Bond Funds **(low/medium risk)**	AAA Rated Pooled cash investment vehicle investing in a range of Government, Financial Institutions and Government Bonds.	Fairly liquid vehicle investing in Bonds with a high average credit rating, will only be used for a relatively small proportion of the fund.
g. Call account deposit accounts with financial institutions (banks and building societies) **(Risk is dependent on credit rating)**	These tend to be moderately low risk investments, but will exhibit higher risks than the categories (a) to (d) above. Whilst there is no risk to value with these types of investments, liquidity is high and investments can be returned at short notice. These will be used to provide the primary liquidity source for Cash Management	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poors. On day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.
h. Term deposits with financial institutions (banks and building societies) **(Low to medium risk**	The risk on these is determined, but will exhibit higher risks than categories (a) to (d) above. Whilst there is no risk to value with these types of	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured

depending on period & credit rating)	investments, liquidity is low and term deposits can only be broken with the agreement of the counterparty, and penalties may apply.	primarily by credit ratings from Fitch, Moody's and Standard and Poors On day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.
i. Certificates of deposits with financial institutions **(risk dependent on credit rating)**	These are short dated marketable securities issued by financial institutions and as such counterparty risk is low, but will exhibit higher risks than categories (a) to (d) above. There is risk to value of capital loss arising from selling ahead of maturity if combined with an adverse movement in interest rates. Liquidity risk will normally be low.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poors. On day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.
j. Structured deposit facilities with banks and building societies (escalating rates, de-escalating rates etc.) **(Low to medium risk depending on period & credit rating)**	These tend to be medium to low risk investments, but will exhibit higher risks than categories (a) to (d) above. Whilst there is no risk to value with these types of investments, liquidity is very low and investments can only be broken with the agreement of the counterparty (penalties may apply).	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poors. On day to day investment dealing with this criteria will be further strengthened by the use of additional market intelligence.
k. Bonds **(Low to medium risk depending on period & credit rating)**	This entails a higher level of risk exposure than gilts and the aim is to achieve a higher rate of return than normally available from gilts. They do have an exposure to movements in market prices of assets held.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, on a hold to maturity basis. Bonds may also carry an explicit Government Guarantee.
l. Floating Rate Notes **(Low to medium risk depending on credit rating)**	These are Bonds on which the rate of interest is established periodically with reference to short term interest rates.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, measured primarily by credit ratings from Fitch, Moody's and Standard and Poors. Will be used in an increasing interest rate environment but only for a limited proportion of the portfolio.
m. Commercial Paper **(Low to medium risk depending on credit rating)**	These are short term promissory notes issued at a discount par. They entail a higher level of risk exposure than gilts and the aim is to achieve a higher rate of return than normally available from gilts. They do have an exposure to movements in market prices of assets held.	The counterparty selection criteria approved above restricts lending only to high quality counterparties, on a hold to maturity basis. They are relatively short maturity.

n. Secured Investments **(relatively low risk due to dual recourse)**	These include Reverse Purchase Agreements (Repo) and Covered Bonds issued by banks and building societies.	Both Repo and Covered Bonds provide opportunities to lower credit risk by having any exposure supported by an enhanced level of high quality collateral such as Gilts in the case of Repo. The lower credit risk is reflected in the Cash Fund being able to invest larger % or value amounts as shown in the criteria for financial institutions in (k).